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In the

Supreme Court of the United States

EVELYN R. KRAFT,

Petitioner,

v.

WASHINGTON MUTUAL BANK, N.A.,
CAL-WESTERN RECONVEYANCE CORPORATION,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

REPLY BRIEF

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EVELYN R. KRAFT,
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WASHINGTON MUTUAL BANK and
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REPLY IN SUPPORT OF EVELYN R. KRAFT'S PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

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1. *Kraft's First Question Is Presented*

Contrary to Washington Mutual's contention that Kraft's first question was not presented below (Opposition at 3-6), the opinion of Judge Philip Brandt for the Ninth Circuit BAP upheld the order annulling the stay in favor of Washington Mutual because Kraft failed to prove her eligibility for bankruptcy protection under the good faith filing doctrine. (10a) ("Kraft neither argued nor cited evidence that her second chapter 13 plan was filed in good faith"). Specifically, Judge Brandt held that Kraft's failure to show changed circumstances between the dismissal of her first and the filing of her

second Chapter 13 case and its conversion to one under Chapter 7 constituted bad faith serial filing under the good faith filing doctrine. (9a-12a)

Judge Brandt acknowledged that Kraft was eligible to be a debtor under Section 109, but held that the bankruptcy court was free to impose eligibility requirements not expressed in Section 109. (12a) Judge Brandt explicitly rejected the argument that *Johnson v. Home State Bank*, 501 U.S. 78, 87 (1991) prohibits courts from penalizing debtors for engaging in forms of serial filing not expressly prohibited by Congress. Judge Brandt limited *Johnson* to the particular form of serial filing at issue in that case. (13a). The Ninth Circuit adopted Judge Brandt's opinion as its own. (2a).

Washington Mutual does not dispute that the Second, Sixth and Ninth Circuits impose on the party opposing annulment the burden of proving the debtor's eligibility for bankruptcy protection. *E.g.*, *Casse v. Key Bank N.A. (In re Casse)*, 198 F.3d 327, 332, 334, 339, 342 (2nd Cir. 1999) (affirming annulment in favor of creditor that foreclosed with notice of stay because husband's filing of a Chapter 13 case after dismissal with prejudice of husband and wife's joint Chapter 11 case with prejudice without first obtaining permission from bankruptcy court violated the good faith filing doctrine); *Trident Assoc. Ltd. Partnership v. Metropolitan Life Ins. Co. (In re Trident Assoc. Ltd. Partnership)*, 52 F.3d 127, 129-132 (6th Cir. 1995) (affirming annulment in favor of creditor that foreclosed with notice of stay because filing after debtor's counsel had stated that he did not know whether debtor intended to file for bankruptcy violated good faith filing doctrine), *cert. denied* 516 U.S. 869 (1995); and Kraft's case (9a-10a) (affirming annulment in favor of creditor that foreclosed with notice of stay because filing of second Chapter 13

case in absence of changed circumstances after dismissal of prior case without 180 day bar violated good faith filing doctrine). Judge Brandt has since repeated this view in *Value T Sales, Inc. v. Mitchell (In re Mitchell)*, 279 B.R. 839, 841 (9th Cir. BAP 2002).

Nor does Washington Mutual dispute that the First, Third and Tenth Circuits do not impose on the party opposing annulment the burden of proving the debtor's eligibility for bankruptcy protection. *E.g.*, *Soares v. Brockton Credit Union (In re Soares)*, 107 F.3d 969, 976 (1st Cir. 1997) ("Treating an action taken in contravention of the automatic stay as void places the burden of validating the action after the fact squarely on the shoulders of the offending creditor."); *Ward. v. Bowest*, 837 F.2d 124, 126 (3rd. Cir. 1988) ("when Charles Ward filed his petition on January 9, 1986, the automatic stay of 11 U.S.C. § 362(a) operated to stay any [enforcement] action"); and *Pro Finance, Inc. v. Spriggs (In re Spriggs)*, 219 B.R. 909, 913 (10th Cir. BAP 1998) (holding that even a serial filer "may rely on the protection afforded under § 362(a)"), *aff'd without published opinion* (10th Cir. 1998).

Washington Mutual does not dispute that the Second, Sixth and Ninth Circuits hold that bankruptcy courts are free to impose eligibility requirements not expressed in Section 109. In *Casse*, 198 F.3d 327, 334, 339; *Trident*, 52 F.3d 127, 130-131; and Kraft's case (12a-13a), the debtor was eligible for bankruptcy protection under Section 109, but found ineligible under the good faith filing doctrine.

Nor does Washington Mutual dispute that the First, Third and Tenth Circuits hold that bankruptcy courts are prohibited from imposing eligibility requirements not expressed in Section 109. *E.g.*, *In re*

Victoria Ltd. Partnership, 187 B.R. 54, 54 (Bankr. D. Mass. 1995) (holding that the good faith filing doctrine is "in conflict with the Bankruptcy Code, its legislative history, Supreme Court precedent, and logic"); *In re Oglesby*, 161 B.R. 917, 924 (Bankr. E.D. Pa. 1993) (citing *Johnson* in holding that "The problem of abusive multiple filings is addressed by 11 U.S.C. § 109(g), and cases not within the precise bounds of that Code section are simply not prohibited."); and *Frieouf v. U.S. (In re Frieouf)*, 938 F.2d 1099, 1103 fn 4 (10th Cir. 1991) ("the bankruptcy court's three-year prohibition against filing a bankruptcy case, which plainly contradicts the 180-day limitation under section 109(g), cannot be sustained under section 105(a)."), *cert. denied* 502 U.S. 1091 (1992).

The Circuits clearly split over whether the party opposing annulment has the burden of proving the debtor's eligibility for bankruptcy protection and over whether bankruptcy courts are free to impose eligibility requirements not expressed in Section 109. These issues were presented in Kraft's case and were dispositive.

2. *The Circuits Split Over Kraft's Second Question*

Washington Mutual asserts that the standard for annulment in all Circuits is one of unlimited discretion. Opposition at 4, 7-8. This is the standard in the Sixth and Ninth Circuits where the courts may look at the "totality of the circumstances." *See* Kraft's case (10a); *National Environmental Waste Corp. v. Riverside (In re National Environmental Waste Corp.)*, 129 F.3d 1052, 1055 (9th Cir. 1997) *cert. denied* 524 U.S. 952(1988); *Mitchell*, 279 B.R. at 841; and *Trident*, 52 F.3d at 131. The First and Tenth Circuits, by contrast, hold

that discretion to annul the stay is very limited. *See Soares*, 107 F.3d at 977 (reversing annulment order because "although courts possess a *limited* discretion to grant retroactive relief from the automatic stay, instances in which the exercise of that discretion is justified are likely to be few and far between") (emphasis added); *Franklin Savings Ass'n v. Office Of Thrift Supervision*, 31 F.3d 1020, 1023 (10th Cir. 1994) ("While district courts and bankruptcy courts have the authority to 'annul' a stay, ... such a result is rare and probably available only to claimants who were honestly ignorant of the bankruptcy stay.").

Washington Mutual asserts that no Circuit requires proof by the creditor of "inability to comply." Opposition at 8. Washington Mutual, however, does not dispute that the First and Tenth Circuit each have denied annulment based on the creditor's ability to comply with the stay. *Soares*, 107 F.3d at 978 (reversing annulment in favor of creditor that had prior notice of the stay); *Franklin Savings Ass'n*, 31 F 3d at 1023 (affirming denial of annulment to creditor that had prior notice of the stay) and *Spriggs*, 219 B.R. 909, 913 (10th Cir. BAP 1998) (refusing annulment to creditor without notice of the stay, because, based on debtor's history of serial filing, creditor should have suspected that debtor had filed another petition prior to scheduled foreclosure sale).

Washington Mutual attempts to distinguish *Soares* by asserting that "*Soares* explicitly allows annulment of the automatic stay [based] solely upon a showing of the debtor's bad faith, and regardless of notice of the stay." Opposition at 8. In fact, the "bad faith" of the debtor referred to *in dicta* in *Soares* meant "bad faith" in giving notice of the bankruptcy and did not refer to "bad faith" in filing the case. Explaining the

role of "bad faith" of the debtor, *Soares* cites *Easley v. Pettibone Michigan Corp.*, 990 F.2d 905, 911 (6th Cir. 1993); *Calder v. Job (In re Calder)*, 907 F.2d 953, 956 (10th Cir. 1990); and *Albany Partners, Ltd v. Westbrook (In re Albany Partners, Ltd.)*, 749 F.2d 670, 675-676 (11th Cir. 1984). In *Easley*, the Sixth Circuit formulated the following standard: "only where the debtor unreasonably withholds notice of the stay and the creditor would be prejudiced if the debtor is able to raise the stay as a defense, or where the debtor is attempting to use the stay unfairly as a shield to avoid an unfavorable result, will the protections of section 362(a) be unavailable to the debtor." *Easley*, 990 F.2d at 911. *Easley* applied this standard to reverse annulment because the debtor "did nothing to lull plaintiffs into believing it would not rely on the stay." *Id.* at 912. *Calder* and *Albany* each affirmed annulment because the debtor, in pursuit of an improper ulterior motive, had withheld notice of the bankruptcy affecting the property in question. *Calder*, 907 F.2d at 956 (Calder caused the creditor's inability to comply with the stay in that "Calder actively litigated the state court action and did not provide notice of the pending Chapter 13 proceeding until just before the state court was to enter a final judgment" against Calder); and *Albany Partners, Ltd.*, 749 F.2d at 675-676 (debtor caused the creditor's inability to comply with the stay by failing to inform the creditor that it claimed an interest in the property scheduled for foreclosure, despite a court order holding that the property belonged to another party). Thus, in the First and Tenth Circuits, a showing by the offending creditor of "inability to comply" is necessary but not sufficient to obtain annulment. At a minimum, the creditor must also show that a calculated bad faith act by the debtor caused the creditor's inability to comply. *Soares*, 107 F.3d at 977; *Spriggs*, 219 B.R. at 913.

In apparent contradiction with its assertion that all Circuits apply a standard of "unlimited discretion," Washington Mutual asserts that all Circuits require a showing of "extreme circumstances" and that there was such a showing in Kraft's case. Opposition at 8-9. In fact, Judge Brandt acknowledged that there were no "extreme circumstances" in Kraft's case, but held that "extreme circumstances " was merely a factor and not a "strict requirement." (10a)

Again contradicting its assertion that all Circuits apply a standard of "unlimited discretion," Washington Mutual asserts that all Circuits require a showing of "entitlement to prospective relief authorizing the enforcement action taken" and that there was such a showing in Kraft's case. Opposition at 9. In fact, Judge Brandt held that such entitlement was only a factor and not a "strict requirement." (10a) Judge Brandt's holding was necessary to the ruling in Kraft's case because Washington Mutual could not have met the standard for prospective relief authorizing the enforcement action taken. An order granting immediate prospective relief without notice requires a showing of "imminent irreparable harm." *See* Section 362(f) and Bankr. Rule 4001. Congress recognized that due process requires *pre*-deprivation notice in all but "extreme circumstances," *e.g.*, *U.S. v. James Daniel Good Real Property*, 510 U.S. 43, 53 (1993), and enacted this requirement directly into Section 362(f) and Bankr. Rule 4001.

The Circuits clearly split over whether the creditor moving for annulment has any burden and, in particular, whether the creditor has the burden of proving one or more of "inability to comply," "extreme circumstances," and entitlement to hypothetical

"prospective relief authorizing the enforcement action taken." These issues were dispositive in Kraft's case.

3. *Krafts Third Question Is Presented*

Contrary to Washington Mutual's contention that Kraft's third question was not presented below (Opposition at 7), Judge Brandt expressly held that the order under Section 549(c) annulling the stay to the date of sale in favor of purchaser Diversified required entry of an order annulling the stay to the date of filing in favor of seller Washington Mutual under Section 362(d). (10a-11a, 14a).

In particular, as to Section 362(d)(1), Judge Brandt held that, by annulling the stay to the date of the September 2, 1998 foreclosure sale, the order in favor of purchaser Diversified under Section 549(c) established that Kraft had filed her second Chapter 13 case in bad faith on April 15, 1998 and required annulment for cause under Section 362(d)(1), namely, bad faith serial filing, in favor of seller Washington Mutual. (10a). As to Section 362(d)(2), Judge Brandt held that the order in favor of purchaser Diversified under Section 549(c) resulted in Kraft and the estate losing all of the $36,634.55 to $70,000.00 of equity in the property and thus required annulment in favor of seller Washington Mutual under Section 362(d)(2) for lack of equity. (10a-11a). As to laches, Judge Brandt held that, in light of the annulment in favor of purchaser Diversified, seller Washington Mutual could rely on the bankruptcy court granting annulment in Washington Mutual's favor at any time and thus laches did not arise from Washington Mutual's failure to move for annulment for two years after the apparent violation and for one year after Kraft had commenced her action for damages under Section

362(h) based on the apparent violation of the stay. (14a).

Kraft's third question concerning whether an order under Section 549(c) upholding a post-petition foreclosure sale requires annulment in favor of the secured creditor seller of the property was presented in Kraft's case and, indeed, was dispositive.

The Circuits split regarding whether entry of an order under Section 549(c) in favor of the purchaser requires annulment in favor of the seller. The Ninth Circuit, espousing a transactional view, holds that, since transactions in violation of the stay are void under *Kalb v. Feuerstein*, 308 U.S. 433, 438 (1940), a rule such as Section 549(c), which declares a particular transaction valid as to one party to the transaction, necessarily absolves all participants in the transaction from liability for violating the stay. The Third Circuit in *Ward*, 837 F.2d at 126, views the avoiding power of the trustee provided for in Section 549(a) as a remedy and Section 549(c) as an exception to that remedy. Under the Third Circuit's view, other remedies such as Section 362(h) are not affected by the loss of the avoiding power vis-à-vis a bona fide purchaser. *See Administrator of Veterans Affairs v. Bernard (In re Bernard)*, 21 B.R. 287, 288 and n. 11 (Bankr. E.D. Pa 1982). In *Mitchell*, the Ninth Circuit BAP discussed the two approaches and explicitly rejected the Third Circuit's approach. 279 B.R. at 844 ("We decline to follow *Ward*.").

CONCLUSION

For these reasons, Kraft respectfully requests that this Court grant a writ of certiorari to the United States Court of Appeals for the Ninth Circuit.

Respectfully submitted,

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